market shares of the larger firms, in accord with their relative importance in competitive interactions.

The Agency divides the spectrum of market concentration as measured by the HHI into three regions that can be broadly characterized as unconcentrated (HHI below 1000), moderately concentrated (HHI between 1000 and 1800), and highly concentrated (HHI above 1800). Although the resulting regions provide a useful framework for merger analysis, the numerical divisions suggest greater precision than is possible with the available economic tools and information. Other things being equal, cases falling just above and just below a threshold present comparable competitive issues.

1.51 General Standards

In evaluating horizontal mergers, the Agency will consider both the post-merger market concentration and the increase in concentration resulting from the merger.[18] Market concentration is a useful indicator of the likely potential competitive effect of a merger. The general standards for horizontal mergers are as follows:

(a) *Post-Merger HHI Below 1000.* The Agency regards markets in this region to be unconcentrated. Mergers resulting in unconcentrated markets are unlikely to have adverse competitive effects and ordinarily require no further analysis.

(b) *Post-Merger HHI Between 1000 and 1800.* The Agency regards markets in this region to be moderately concentrated. Mergers producing an increase in the HHI of less than 100 points in moderately concentrated markets post-merger are unlikely to have adverse competitive consequences and ordinarily require no further analysis. Mergers producing an increase in the HHI of more than 100 points in moderately concentrated markets post-merger potentially raise significant competitive concerns depending on the factors set forth in sections 2–5 of the Guidelines.

(c) *Post-Merger HHI Above 1800.* The Agency regards markets in this region to be highly concentrated. Mergers producing an increase in the HHI of less than 50 points, even in highly concentrated markets post-merger, are unlikely to have adverse competitive consequences and ordinarily require no further analysis. Mergers producing an increase in the HHI of more than 50 points in highly concentrated markets post-merger potentially raise significant competitive concerns, depending on the factors set forth in sections 2–5 of the Guidelines. Where the post-merger HHI exceeds 1800, it will be presumed that mergers producing an increase in the HHI of more than 100 points are likely to create or enhance market power or facilitate its exercise. The presumption may be overcome by a showing that factors set forth in sections 2–5 of the Guidelines make it unlikely that the merger will create or enhance market power or facilitate its exercise, in light of market concentration and market shares.

1.52 Factors Affecting the Significance of Market Shares and Concentration

The post-merger level of market concentration and the change in concentration resulting from a merger affect the degree to which a merger raises competitive concerns. However, in some situations, market share and market concentration data may either understate or overstate the likely future competitive significance of a firm or firms in the market or the impact of a merger. The following are examples of such situations.

1.521 Changing Market Conditions

Market concentration and market share data of necessity are based on historical evidence. However, recent or ongoing changes in the market may indicate that the current market share of a particular firm either understates or overstates the firm's future competitive significance. For example, if a new technology that is important to long-term competitive viability is available to other firms in the market, but is not available to a particular firm, the Agency may conclude that the historical market share of that firm overstates its future competitive significance. The Agency will consider reasonably predictable effects of recent or ongoing changes in market conditions in interpreting market concentration and market share data.

1.522 Degree of Difference Between the Products and Locations in the Market and Substitutes Outside the Market

All else equal, the magnitude of potential competitive harm from a merger is greater if a hypothetical monopolist would raise price within the relevant market by substantially more than a "small but significant and nontransitory" amount. This may occur when the demand substitutes outside the relevant market, as a group, are not close substitutes for the products and locations within the relevant market. There thus may be a wide gap in the chain of demand substitutes at the edge of the product and geographic market. Under such circumstances, more market power is at stake in the relevant market than in a market in which a hypothetical monopolist would raise price by exactly five percent.

2. The Potential Adverse Competitive Effects of Mergers

2.0 Overview

Other things being equal, market concentration affects the likelihood that one firm, or a small group of firms, could successfully exercise market power. The smaller the percentage of total supply that a firm controls, the more severely it must restrict its own output in order to produce a given price increase, and the less likely it is that an output restriction will be profitable. If collective action is necessary for the exercise of market power, as the number of firms necessary to control a given percentage of total supply decreases, the difficulties and costs of reaching and enforcing an understanding with respect to the control of that supply might be reduced. However, market share and concentration data provide only the starting point for analyzing the competitive impact of a merger. Before determining whether to challenge a merger, the Agency also will assess the other market factors that pertain to competitive effects, as well as entry, efficiencies and failure.

This section considers some of the potential adverse competitive effects of mergers and the factors in addition to market concentration relevant to each. Because an individual merger may threaten to harm competition through more than one of these effects, mergers will be analyzed in terms of as many potential adverse competitive effects as are appropriate. Entry, efficiencies, and failure are treated in Sections 3–5.

2.1 Lessening of Competition Through Coordinated Interaction

A merger may diminish competition by enabling the firms selling in the relevant market more likely, more successfully, or more completely to engage in coordinated interaction that harms consumers. Coordinated interaction is comprised of actions by a group of firms that are profitable for each of them only as a result of the accommodating reactions of the others.

[18] The increase in concentration as measured by the HHI can be calculated independently of the overall market concentration by doubling the product of the market shares of the merging firms. For example, the merger of firms with shares of 5 percent and 10 percent of the market would increase the HHI by 100 ($5 \times 10 \times 2 = 100$). The explanation for this technique is as follows: In calculating the HHI before the merger, the market shares of the merging firms are squared individually: $(a)^2 + (b)^2$. After the merger, the sum of those shares would be squared: $(a + b)^2$, which equals $a^2 + 2ab + b^2$. The increase in the HHI therefore is represented by $2ab$.

behavior includes tacit or express collusion, and may or may not be lawful in and of itself.

Successful coordinated interaction entails reaching terms of coordination that are profitable to the firms involved and an ability to detect and punish deviations that would undermine the coordinated interaction. Detection and punishment of deviations ensure that coordinating firms will find it more profitable to adhere to the terms of coordination than to pursue short-term profits from deviating, given the costs of reprisal. In this phase of the analysis, the Agency will examine the extent to which post-merger market conditions are conducive to reaching terms of coordination, detecting deviations from those terms, and punishing such deviations. Depending upon the circumstances, the following market factors, among others, may be relevant: the availability of key information concerning market conditions, transactions and individual competitors; the extent of firm and product heterogeneity; pricing or marketing practices typically employed by firms in the market; the characteristics of buyers and sellers; and the characteristics of typical transactions.

Certain market conditions that are conducive to reaching terms of coordination also may be conducive to detecting or punishing deviations from those terms. For example, the extent of information available to firms in the market, or the extent of homogeneity, may be relevant to both the ability to reach terms of coordination and to detect or punish deviations from those terms. The extent to which any specific market condition will be relevant to one or more of the conditions necessary to coordinated interaction will depend on the circumstances of the particular case.

It is likely that market conditions are conducive to coordinated interaction when the firms in the market previously have engaged in express collusion and when the salient characteristics of the market have not changed appreciably since the most recent such incident. Previous express collusion in another geographic market will have the same weight when the salient characteristics of that other market at the time of the collusion are comparable to those in the relevant market.

In analyzing the effect of a particular merger on coordinated interaction, the Agency is mindful of the difficulties of predicting likely future behavior based on the types of incomplete and sometimes contradictory information typically generated in merger investigations. Whether a merger is likely to diminish competition by enabling firms more likely, more successfully or more completely to engage in coordinated interaction depends on whether market conditions, on the whole, are conducive to reaching terms of coordination and detecting and punishing deviations from those terms.

2.11 Conditions Conducive to Reaching Terms of Coordination

Firms coordinating their interactions need not reach complex terms concerning the allocation of the market output across firms or the level of the market prices but may, instead, follow simple terms such as a common price, fixed price differentials, stable market shares, or customer or territorial restrictions. Terms of coordination need not perfectly achieve the monopoly outcome in order to be harmful to consumers. Instead, the terms of coordination may be imperfect and incomplete—inasmuch as they omit some market participants, omit some dimensions of competition, omit some customers, yield elevated prices short of monopoly levels, or lapse into episodic price wars—and still result in significant competitive harm. At some point, however, imperfections cause the profitability of abiding by the terms of coordination to decrease and, depending on their extent, may make coordinated interaction unlikely in the first instance.

Market conditions may be conducive to or hinder reaching terms of coordination. For example, reaching terms of coordination may be facilitated by product or firm homogeneity and by existing practices among firms, practices not necessarily themselves antitrust violations, such as standardization of pricing or product variables on which firms could compete. Key information about rival firms and the market may also facilitate reaching terms of coordination. Conversely, reaching terms of coordination may be limited or impeded by product heterogeneity or by firms having substantially incomplete information about the conditions and prospects of their rivals' businesses, perhaps because of important differences among their current business operations. In addition, reaching terms of coordination may be limited or impeded by firm heterogeneity, for example, differences in vertical integration or the production of another product that tends to be used together with the relevant product.

2.12 Conditions Conducive to Detecting and Punishing Deviations

Where market conditions are conducive to timely detection and punishment of significant deviations, a firm will find it more profitable to abide by the terms of coordination than to deviate from them. Deviation from the terms of coordination will be deterred where the threat of punishment is credible. Credible punishment, however, may not need to be any more complex than temporary abandonment of the terms of coordination by other firms in the market.

Where detection and punishment likely would be rapid, incentives to deviate are diminished and coordination is likely to be successful. The detection and punishment of deviations may be facilitated by existing practices among firms themselves, not necessarily antitrust violations, and by the characteristics of typical transactions. For example, if key information about specific transactions or individual price or output levels is available routinely to competitors, it may be difficult for a firm to deviate secretly. If orders for the relevant product are frequent, regular and small relative to the total output of a firm in a market, it may be difficult for the firm to deviate in a substantial way without the knowledge of rivals and without the opportunity for rivals to react. If demand or cost fluctuations are relatively infrequent and small, deviations may be relatively easy to deter.

By contrast, where detection or punishment is likely to be slow, incentives to deviate are enhanced and coordinated interaction is unlikely to be successful. If demand or cost fluctuations are relatively frequent and large, deviations may be relatively difficult to distinguish from these other sources of market price fluctuations, and, in consequence, deviations may be relatively difficult to deter.

In certain circumstances, buyer characteristics and the nature of the procurement process may affect the incentives to deviate from terms of coordination. Buyer size alone is not the determining characteristic. Where large buyers likely would engage in long-term contracting, so that the sales covered by such contracts can be large relative to the total output of a firm in the market, firms may have the incentive to deviate. However, this only can be accomplished where the duration, volume and profitability of the business covered by such contracts are sufficiently large as to make deviation more profitable in the long term than honoring the terms of coordination, and buyers likely would switch suppliers.

In some circumstances, coordinated interaction can be effectively prevented or limited by maverick firms—firms that have a greater economic incentive to deviate from the terms of coordination than do most of their rivals (*e.g.*, firms that are unusually disruptive and competitive influences in the market). Consequently, acquisition of a maverick firm is one way in which a merger may make coordinated interaction more likely, more successful, or more complete. For example, in a market where capacity constraints are significant for many competitors, a firm is more likely to be a maverick the greater is its excess or divertible capacity in relation to its sales or its total capacity, and the lower are its direct and opportunity costs of expanding sales in the relevant market.[19] This is so because a firm's incentive to deviate from price-elevating and output-limiting terms of coordination is greater the more the firm is able profitably to expand its output as a proportion of the sales it would obtain if it adhered to the terms of coordination and the smaller is the base of sales on which it enjoys elevated profits prior to the price-cutting deviation.[20] A firm also may be a maverick if it has an unusual ability secretly to expand its sales in relation to the sales it would obtain if it adhered to the terms of coordination. This ability might arise from opportunities to expand captive production for a downstream affiliate.

2.2 *Lessening of Competition Through Unilateral Effects*

A merger may diminish competition even if it does not lead to increased likelihood of successful coordinated interaction, because merging firms may find it profitable to alter their behavior unilaterally following the acquisition by elevating price and suppressing output. Unilateral competitive effects can arise in a variety of different settings. In each setting, particular other factors describing the relevant market affect the likelihood of unilateral competitive effects. The settings differ by the primary characteristics that distinguish firms and shape the nature of their competition.

2.21 Firms Distinguished Primarily by Differentiated Products

In some markets the products are differentiated, so that products sold by different participants in the market are not perfect substitutes for one another. Moreover, different products in the market may vary in the degree of their substitutability for one another. In this setting, competition may be non-uniform (*i.e.*, localized), so that individual sellers compete more directly with those rivals selling closer substitutes.[21]

A merger between firms in a market for differentiated products may diminish competition by enabling the merged firm to profit by unilaterally raising the price of one or both products above the premerger level. Some of the sales loss due to the price rise merely will be diverted to the product of the merger partner and, depending on relative margins, capturing such sales loss through merger may make the price increase profitable even though it would not have been profitable premerger. Substantial unilateral price elevation in a market for differentiated products requires that there be a significant share of sales in the market accounted for by consumers who regard the products of the merging firms as their first and second choices, and that repositioning of the non-parties' product lines to replace the localized competition lost through the merger be unlikely. The price rise will be greater the closer substitutes are the products of the merging firms, *i.e.*, the more the buyers of one product consider the other product to be their next choice.

2.211 Closeness of the Products of the Merging Firms

The market concentration measures articulated in Section 1 may help assess the extent of the likely competitive effect from a unilateral price elevation by the merged firm notwithstanding the fact that the affected products are differentiated. The market concentration measures provide a measure of this effect if each product's market share is reflective of not only its relative appeal as a first choice to consumers of the merging firms' products but also its relative appeal as a second choice, and hence as a competitive constraint to the first choice.[22] Where this circumstance holds, market concentration data fall outside the safeharbor regions of section 1.5, and the merging firms have a combined market share of at least thirty-five percent, the Agency will presume that a significant share of sales in the market are accounted for by consumers who regard the products of the merging firms as their first and second choices.

Purchasers of one of the merging firms' products may be more or less likely to make the other their second choice than market shares alone would indicate. The market shares of the merging firms' products may understate the competitive effect of concern, when, for example, the products of the merging firms are relatively more similar in their various attributes to one another than to other products in the relevant market. On the other hand, the market shares alone may overstate the competitive effects of concern when, for example, the relevant products are less similar in their attributes to one another than to other products in the relevant market.

Where market concentration data fall outside the safeharbor regions of section 1.5, the merging firms have a combined market share of at least thirty-five percent, and where data on product attributes and relative product appeal show that a significant share of purchasers of one merging firm's product regard the other as their second choice, then market share data may be relied upon to demonstrate that there is a significant share of sales in the market accounted for by consumers who would be adversely affected by the merger.

2.212 Ability of Rival Sellers to Replace Lost Competition

A merger is not likely to lead to unilateral elevation of prices of differentiated products if, in response to such an effect, rival sellers likely would replace any localized competition lost through the merger by repositioning their product lines.[23]

[19] But excess capacity in the hands of non-maverick firms may be a potent weapon with which to punish deviations from the terms of coordination.

[20] Similarly, in a market where product design or quality is significant, a firm is more likely to be an effective maverick the greater is the sales potential of its products among customers of its rivals, in relation to the sales it would obtain if it adhered to the terms of coordination. The likelihood of expansion responses by a maverick will be analyzed in the same fashion as uncommitted entry or committed entry (see sections 1.3 and 3) depending on the significance of the sunk costs entailed in expansion.

[21] Similarly, in some markets sellers are primarily distinguished by their relative advantages in serving different buyers or groups of buyers, and buyers negotiate individually with sellers. Here, for example, sellers may formally bid against one another for the business of a buyer, or each buyer may elicit individual price quotes from multiple sellers. A seller may find it relatively inexpensive to meet the demands of particular buyers or types of buyers, and relatively expensive to meet others' demands. Competition, again, may be localized: sellers compete more directly with those rivals having similar relative advantages in serving particular buyers or groups of buyers. For example, in open outcry auctions, price is determined by the cost of the second lowest-cost seller. A merger involving the first and second lowest-cost sellers could cause prices to rise to the constraining level of the next lowest-cost seller.

[22] Information about consumers' actual first and second product choices may be provided by marketing surveys, information from bidding structures, or normal course of business documents from industry participants.

[23] The timeliness and likelihood of repositioning responses will be analyzed using the same methodology as used in analyzing uncommitted entry or committed entry (see sections 1.3 and 3), depending on the significance of the sunk costs entailed in repositioning.

in markets where it is costly for buyers to evaluate product quality, buyers who consider purchasing from both merging parties may limit the total number of sellers they consider. If either of the merging firms would be replaced in such buyers' consideration by an equally competitive seller not formerly considered, then the merger is not likely to lead to a unilateral elevation of prices.

2.22 Firms Distinguished Primarily by Their Capacities

Where products are relatively undifferentiated and capacity primarily distinguishes firms and shapes the nature of their competition, the merged firm may find it profitable unilaterally to raise price and suppress output. The merger provides the merged firm a larger base of sales on which to enjoy the resulting price rise and also eliminates a competitor to which customers otherwise would have diverted their sales. Where the merging firms have a combined market share of at least thirty-five percent, merged firms may find it profitable to raise price and reduce joint output below the sum of their premerger outputs because the lost markups on the foregone sales may be outweighed by the resulting price increase on the merged base of sales.

This unilateral effect is unlikely unless a sufficiently large number of the merged firm's customers would not be able to find economical alternative sources of supply, *i.e.*, competitors of the merged firm likely would not respond to the price increase and output reduction by the merged firm with increases in their own outputs sufficient in the aggregate to make the unilateral action of the merged firm unprofitable. Such non-party expansion is unlikely if those firms face binding capacity constraints that could not be economically relaxed within two years or if existing excess capacity is significantly more costly to operate than capacity currently in use.[24]

3. Entry Analysis

3.0 Overview

A merger is not likely to create or enhance market power or to facilitate its exercise, if entry into the market is so easy that market participants, after the merger, either collectively or unilaterally could not profitably maintain a price increase above premerger levels. Such entry likely will deter an anticompetitive merger in its incipiency, or deter or counteract the competitive effects of concern.

Entry is that easy if entry would be timely, likely, and sufficient in its magnitude, character and scope to deter or counteract the competitive effects of concern. In markets where entry is that easy (*i.e.*, where entry passes these tests of timeliness, likelihood, and sufficiency), the merger raises no antitrust concern and ordinarily requires no further analysis.

The committed entry treated in this section is defined as new competition that requires expenditure of significant sunk costs of entry and exit.[25] The Agency employs a three step methodology to assess whether committed entry would deter or counteract a competitive effect of concern.

The first step assesses whether entry can achieve significant market impact within a timely period. If significant market impact would require a longer period, entry will not deter or counteract the competitive effect of concern.

The second step assesses whether committed entry would be a profitable and, hence, a likely response to a merger having competitive effects of concern. Firms considering entry that requires significant sunk costs must evaluate the profitability of the entry on the basis of long term participation in the market, because the underlying assets will be committed to the market until they are economically depreciated. Entry that is sufficient to counteract the competitive effects of concern will cause prices to fall to their premerger levels or lower. Thus, the profitability of such committed entry must be determined on the basis of premerger market prices over the long-term.

A merger having anticompetitive effects can attract committed entry, profitable at premerger prices, that would not have occurred premerger at these same prices. But following the merger, the reduction in industry output and increase in prices associated with the competitive effect of concern may allow the same entry to occur without driving market prices below premerger levels. After a merger that results in decreased output and increased prices, the likely sales opportunities available to entrants at premerger prices will be larger than they were premerger, larger by the output reduction caused by the merger. If entry could be profitable at premerger prices without exceeding the likely sales opportunities—opportunities that include pre-existing pertinent factors as well as the merger-induced output reduction—then such entry is likely in response to the merger.

The third step assesses whether timely and likely entry would be sufficient to return market prices to their premerger levels. This end may be accomplished either through multiple entry or individual entry at a sufficient scale. Entry may not be sufficient, even though timely and likely, where the constraints on availability of essential assets, due to incumbent control, makes it impossible for entry profitably to achieve the necessary level of sales. Also, the character and scope of entrants' products might not be fully responsive to the localized sales opportunities created by the removal of direct competition among sellers of differentiated products. In assessing whether entry will be timely, likely, and sufficient, the Agency recognizes that precise and detailed information may be difficult or impossible to obtain. In such instances, the Agency will rely on all available evidence bearing on whether entry will satisfy the conditions of timeliness, likelihood, and sufficiency.

3.1 Entry Alternatives

The Agency will examine the timeliness, likelihood, and sufficiency of the means of entry (entry alternatives) a potential entrant might practically employ, without attempting to identify who might be potential entrants. An entry alternative is defined by the actions the firm must take in order to produce and sell in the market. All phases of the entry effort will be considered, including, where relevant, planning, design, and management; permitting, licensing, and other approvals; construction, debugging, and operation of production facilities; and promotion (including necessary introductory discounts), marketing, distribution, and satisfaction of customer testing and qualification requirements.[26] Recent examples of entry, whether successful or unsuccessful, may provide a useful starting point for identifying the necessary actions, time requirements, and characteristics of possible entry alternatives.

3.2 Timeliness of Entry

In order to deter or counteract the competitive effects of concern, entrants quickly must achieve a significant impact on price in the relevant market. The Agency generally will consider

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[24] The timeliness and likelihood of non-party expansion will be analyzed using the same methodology as used in analyzing uncommitted or committed entry (*see* Sections 1.3 and 3) depending on the significance of the sunk costs entailed in expansion.

[25] Supply responses that require less than one year and insignificant sunk costs to effectuate are analyzed as uncommitted entry in section 1.3.

[26] Many of these phases may be undertaken simultaneously.

timely only those committed entry alternatives that can be achieved within two years from initial planning to significant market impact.[27] Where the relevant product is a durable good, consumers, in response to a significant commitment to entry, may defer purchases by making additional investments to extend the useful life of previously purchased goods and in this way deter or counteract for a time the competitive effects of concern. In these circumstances, if entry only can occur outside of the two year period, the Agency will consider entry to be timely so long as it would deter or counteract the competitive effects of concern within the two year period and subsequently.

3.3 Likelihood of Entry

An entry alternative is likely if it would be profitable at premerger prices, and if such prices could be secured by the entrant.[28] The committed entrant will be unable to secure prices at premerger levels if its output is too large for the market to absorb without depressing prices further. Thus, entry is unlikely if the minimum viable scale is larger than the likely sales opportunity available to entrants.

Minimum viable scale is the smallest average annual level of sales that the committed entrant must persistently achieve for profitability at premerger prices.[29] Minimum viable scale is a function of expected revenues, based upon premerger prices,[30] and all categories of costs associated with the entry alternative, including an appropriate rate of return on invested capital given that entry could fail and sunk costs, if any, will be lost.[31]

Sources of sales opportunities available to entrants include: (a) The output reduction associated with the competitive effect of concern,[32] (b) entrants' ability to capture a share of reasonably expected growth in market demand,[33] (c) entrants' ability securely to divert sales from incumbents, for example, through vertical integration or through forward contracting, and (d) any additional anticipated contraction in incumbents' output in response to entry.[34] Factors that reduce the sales opportunities available to entrants include: (a) The prospect that an entrant will share in a reasonably expected decline in market demand, (b) the exclusion of an entrant from a portion of the market over the long term because of vertical integration or forward contracting by incumbents, and (c) any anticipated sales expansion by incumbents in reaction to entry, either generalized or targeted at customers approached by the entrant, that utilizes prior irreversible investments in excess production capacity. Demand growth or decline will be viewed as relevant only if total market demand is projected to experience long-lasting change during at least the two year period following the competitive effect of concern.

3.4 Sufficiency of Entry

Inasmuch as multiple entry generally is possible and individual entrants may flexibly choose their scale, committed entry generally will be sufficient to deter or counteract the competitive effects of concern whenever entry is likely under the analysis of section 3.3. However, entry, although likely, will not be sufficient if, as a result of incumbent control, the tangible and intangible assets required for entry are not adequately available for entrants to respond fully to their sales opportunities. In addition, where the competitive effect of concern is not uniform across the relevant market, in order for entry to be sufficient, the character and scope of entrants' products must be responsive to the localized sales opportunities that include the output reduction associated with the competitive effect of concern. For example, where the concern is unilateral price elevation as a result of a merger between producers of differentiated products, entry, in order to be sufficient, must involve a product so close to the products of the merging firms that the merged firm will be unable to internalize enough of the sales loss due to the price rise, rendering the price increase unprofitable.

4. Efficiencies

The primary benefit of mergers to the economy is their efficiency-enhancing potential, which can increase the competitiveness of firms and result in lower prices to consumers. Because the antitrust laws, and thus the standards of the Guidelines, are designed to proscribe only mergers that present a significant danger to competition, they do not present an obstacle to most mergers. As a consequence, in the majority of cases, the Guidelines will allow firms to achieve available efficiencies through mergers without interference from the Agency.

Some mergers that the Agency otherwise might challenge may be reasonably necessary to achieve significant net efficiencies. Cognizable efficiencies include, but are not limited to, achieving economies of scale, better integration of production facilities, plant specialization, lower transportation costs, and similar efficiencies relating to specific manufacturing, servicing, or distribution operations of the merging firms. The Agency may also consider claimed efficiencies resulting from reductions in general selling, administrative, and overhead expenses, or that otherwise do not relate to specific manufacturing, servicing, or distribution operations of the merging firms, although, as a practical matter, these types of efficiencies may be difficult to demonstrate. In addition, the Agency will reject claims of efficiencies if equivalent or comparable savings can reasonably be achieved by the parties through other means. The expected net efficiencies must be greater the more significant are the competitive risks identified in sections 1–3.

5. Failure and Exiting Assets

5.0 Overview

Notwithstanding the analysis of sections 1–4 of the Guidelines, a merger is not likely to create or enhance market power or to facilitate its exercise, if imminent failure, as defined below, of one of the merging firms would cause the assets of that firm to exit the relevant market. In such circumstances

[27] Firms which have committed to entering the market prior to the merger generally will be included in the measurement of the market. Only committed entry or adjustments to pre-existing entry plans that are induced by the merger will be considered as possibly deterring or counteracting the competitive effects of concern.

[28] Where conditions indicate that entry may be profitable at prices below premerger levels, the Agency will assess the likelihood of entry at the lowest price at which such entry would be profitable.

[29] The concept of minimum viable scale ("MVS") differs from the concept of minimum efficient scale ("MES"). While MES is the smallest scale at which average costs are minimized, MVS is the smallest scale at which average costs equal the premerger price.

[30] The expected path of future prices, absent the merger, may be used if future price changes can be predicted with reasonable reliability.

[31] The minimum viable scale of an entry alternative will be relatively large when the fixed costs of entry are large, when the fixed costs of entry are largely sunk, when the marginal costs of production are high at low levels of output, and when a plant is underutilized for a long time because of delays in achieving market acceptance.

[32] Five percent of total market sales typically is used because where a monopolist profitably would raise price by five percent or more across the entire relevant market, it is likely that the accompanying reduction in sales would be no less than five percent.

[33] Entrants' anticipated share of growth in demand depends on incumbents' capacity constraints and irreversible investments in capacity expansion, as well as on the relative appeal, acceptability and reputation of incumbents' and entrants' products to the new demand.

[34] For example, in a bidding market where all bidders are on equal footing, the market share of incumbents will contract as a result of entry.

...merger performance in the relevant ...ket may be no worse than market ...rmance had the merger been ...ked and the assets left the market.

...Failing Firm

...merger is not likely to create or ...nce market power or facilitate its ...se if the following circumstances ...met: (1) The allegedly failing firm ...ld be unable to meet its financial ...gations in the near future; (2) it ...ld not be able to reorganize ...essfully under Chapter 11 of the ...ruptcy Act; [35] (3) it has made ...ccessful good-faith efforts to elicit ...onable alternative offers of ...uisition of the assets of the failing firm [36] that would both keep its tangible and intangible assets in the relevant market and pose a less severe danger to competition than does the proposed merger; and (4) absent the acquisition, the assets of the failing firm would exit the relevant market.

5.2 Failing Division

A similar argument can be made for "failing" divisions as for failing firms. First, upon applying appropriate cost allocation rules, the division must have a negative cash flow on an operating basis. Second, absent the acquisition, it must be that the assets of the division would exit the relevant market in the near future if not sold. Due to the ability of the parent firm to allocate costs, revenues, and intracompany transactions among itself and its subsidiaries and divisions, the Agency will require evidence, not based solely on management plans that could be prepared solely for the purpose of demonstrating negative cash flow or the prospect of exit from the relevant market. Third, the owner of the failing division also must have complied with the competitively-preferable purchaser requirement of section 5.1.

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[35] 11 U.S.C. 1101–1174 (1988).

[36] Any offer to purchase the assets of the failing firm for a price above the liquidation value of those assets—the highest valued use outside the relevant market or equivalent offer to purchase the stock of the failing firm—will be regarded as a reasonable alternative offer.

AT&T Earnings Commentary

April 20, 1998

First Quarter Earnings From Continuing Operations Were $0.80 Per Share

Earnings Adjusted for Gains and Charges Were $0.77 Per Share

FIRST QUARTER 1998 SUMMARY

- *AT&T's first quarter earnings from continuing operations* were $0.77 per share on a diluted basis. This excludes gains totaling $0.26 per share from the sales of AT&T Solutions Customer Care (ASCC) and AT&T's holdings of LIN Television Corp. Also excluded is a charge of $0.23 per share reflecting AT&T's decision not to pursue the sale of local service on a total service resale basis.
- *Earnings from continuing operations* were $0.80 per share on a diluted basis, an increase of 19% from $0.67 in the first quarter of 1997. Consolidated earnings per share were $0.81, up 17% from $0.69 per share in the year-ago quarter. The $0.81 included $0.01 in earnings per share from discontinued operations, reflecting the operating results of AT&T Universal Card, which was sold to Citibank on April 2, 1998.
- *Revenue* increased 0.7% compared to the first quarter of 1997 driven by growth in business services revenue. The year-over-year revenue growth rates for each of AT&T's three largest segments—business services, consumer services, and wireless services—improved compared to the fourth quarter of 1997.
- *Earnings before interest, taxes, depreciation and amortization (EBITDA)* increased 13.3% to $3.1 billion. Excluding the non-cash write-down of local assets mentioned above, EBITDA increased 35% to $3.7 billion. The increase was primarily due to the sales of ASCC and LIN Television Corp. SG&A expense declined $142 million or 3.9% as part of AT&T's commitment to reduce SG&A expense by $1.6 billion in 1998.
- *Business services* revenue, including revenue from local service, increased 4.5% year-over-year, driven by continued strong growth in data services revenue. EBIT from business services increased 1.1%; however, excluding the gain on the sale of AT&T Skynet in 1Q97 EBIT was up 10.0% compared to the year-ago quarter.
- *Consumer services* revenue, including local service revenue, decreased 5.1% reflecting the flow-through of access rate reductions to customers and the targeted migration of customers to optional calling plans. EBIT declined 13.0% from 4Q97 as a result of the traditionally higher level of marketing in the first quarter as well as normal post-holiday revenue trends. EBIT from consumer services increased 11.8% compared to 1Q97.
- *Wireless services* revenue increased 7.0% as consolidated subscribers increased 16.9% to 6.2 million. EBITDA from core wireless services increased slightly in spite of AT&T's aggressive

migration of customers to digital service. Over one-third of AT&T's consolidated wireless subscriber base now uses digital service.

Quarter at a Glance

Growth Compared to:	1Q97	4Q97
Business Services Revenue	4.5%	3.4%
Consumer Services Revenue	(5.1)%	(2.1)%
Wireless Services Revenue	7.0%	(3.7)%
Business Services EBIT	1.1%	(2.6)%
Consumer Services EBIT	11.8%	(13.0)%
Wireless Services EBITDA	2.2%	5.8%
Long-distance Revenue	(0.8)%	0.6%
Long-distance Volume	4.9%	2.3%

AT&T First Quarter Highlights

Total Revenue	$12.6 Billion
SG&A as % of Revenue	27.3%
EBITDA	$3.1 Billion
Net Income	$1.3 Billion
As of 3/31/98:	
YTD Reduction in Employees	4,500
Debt/Total Equity	28.2%
YTD Stock Price Change	+ 7.2%

Earnings Per Share Recap

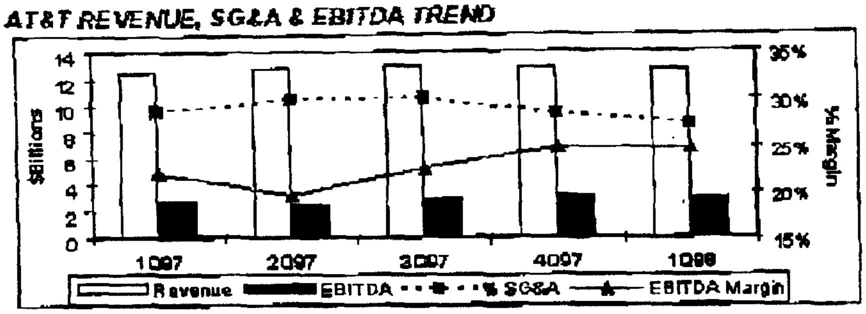
EPS on a diluted basis from:	1Q98	4Q97	3Q97	2Q97
Continuing Operations*	$0.80	$0.81	$0.69	$0.57
Discontinued Operations Including Gains**	0.01	-	0.06	0.02
Consolidated AT&T	$0.81	$0.81	$0.75	$0.59

*1Q98 includes $0.26 in gains on sales of AT&T Solutions Customer Care and LIN-TV, and $(0.23) for the write-down of assets associated with local service resale. 1Q97 includes a gain of $0.04 per share on the sale of AT&T Skynet, $0.04 for the reversal of pre-1995 restructuring reserves, and $(0.06) to exit the 2-way messaging initiative.

**3Q97 includes a gain of $0.04 on the sale of AT&T's submarine systems business.

Income Statement Discussion

AT&T REVENUE, SG&A & EBITDA TREND



AT&T 1st Quarter Summary				
	1Q98	1Q97	Yr/Yr %	4Q97
Revenue	$12,631	$12,548	0.7%	$12,713
SG&A/Revenue	27.3%	28.6%	(130)b.p.	28.3%
EBITDA	3,121	2,753	13.3%	3,132
EBITDA Excluding Gain & Charges	*3,055*	*2,636*	*15.9%*	*3,132*
EBIT	2,090	1,807	15.7%	2,108
EBIT Excluding Gain & Charges	*2,024*	*1,770*	*14.4%*	*2,108*

Revenue

Total revenue increased $83 million or 0.7% compared to 1Q97 as increases in revenue from business services, other/corporate revenues and wireless services revenues were offset by a decrease in revenue from consumer services. Long-distance revenue was down 0.8% compared to 1Q97, while calling volume increased 4.9%. The gap between revenue and volume growth improved to negative 5.7%, as pricing in business markets firmed and free minutes, which continue to be used as a customer incentive, no longer affected the year-over-year revenue growth rate for consumer services. A detailed discussion of revenue performance by segment begins on page 5.

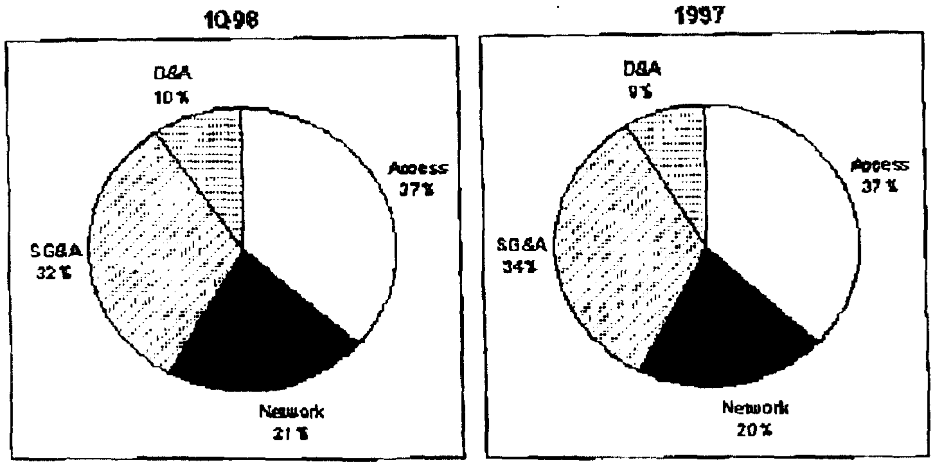
Operating Expenses

Access and other interconnection expenses decreased 8.1% compared to 1Q97. The decline relates primarily to lower international settlement rates, reductions in per-minute access charges, and AT&T's continuing efforts to manage access and interconnection costs. Reductions in per-minute access expenses were partially offset by Primary Interexchange Carrier Charges (PICC), AT&T's contributions to the Universal Service Fund (USF), and volume increases. Access and other interconnection expenses were 34.7% of long-distance services revenue this quarter, compared to 37.5% in 1Q97 and 34.3% in 4Q97.

Network and other communications services expenses increased 6.1% compared to 1Q97. The increase was driven primarily by costs associated with compensation to payphone operators. Recovery of the 28.4-cents-per-call payphone charge is built into interstate pricing for business customers and is collected from calling card users as a surcharge on customer bills. Higher costs related to increasing data traffic on the AT&T network and equipment sales also contributed to the increase. The 1Q97 reversal of pre-1995 restructuring charges also contributed to the increase, while the 1Q97 charge to exit the two-way messaging business and a significant decline in uncollectibles partially offset the increases.

Depreciation and amortization expenses increased 9.2% compared to 1Q97. Excluding the $80 million impact of charges to exit the two-way messaging business in 1Q97, depreciation and amortization expense increased 19.5%. The higher level of expense was driven by increased capital expenditures. Capital spending continues to be directed primarily at AT&T's long-distance network, including the deployment of SONET technology. AT&T expects to finish its three-year SONET program in 1998 with the completion of more than 50 SONET rings. The continuing expansion and upgrade of AT&T's wireless network also contributed to the increase.

DISTRIBUTION OF EXPENSE (Not Including 1Q98 Asset Impairment Charge)



Selling, general and administrative expenses were down $142 million, or 3.9% from 1Q97. SG&A was 27.3% of total revenue, down from 28.6% in the year-ago quarter and 28.3% in 4Q97. The reduced level of expenses reflects AT&T's efforts to achieve a best-in-class cost structure, including targeting the removal of $1.6 billion in SG&A expense from the business in 1998 and a 22% SG&A/revenue ratio by the end of 1999. Cost savings were achieved in a number of areas across the business in the first quarter. In particular, the company realized savings on direct mail and telemarketing to consumers, including efforts to focus on targeted customer segments. Lower marketing and sales costs in business markets, achieved largely through consolidation of functions and reductions of support staff headcount, also contributed to the decline, along with reductions in corporate staff. These reductions were partially offset by expenses related to new wireless businesses.

AT&T has announced a plan to reduce total headcount by 15,000 – 18,000 as a part of the company's overall cost reduction program. The company expects to generate the majority of these reductions from the voluntary force reduction offer that is being offered to eligible employees in the second quarter. Employees are expected to leave the payroll in stages throughout the remainder of 1998, with a significant portion exiting the business by June 30. As of March 31, approximately 4,500 employees had left the business as a result of other force management efforts.

AT&T recorded an *asset impairment and restructuring charge* of $601 million reflecting the decision not to pursue the sale of local service on a Total Service Resale (TSR) basis. The pre-tax charge is comprised primarily of write-downs of software related to ordering, provisioning and billing for resold local service.

Other income statement items

Other income - net was $700 million in the first quarter, up $532 million from 1Q97. The increase resulted primarily from gains on the sales of AT&T Solutions Customer Care (ASCC) and AT&T's holdings of LIN Television Corp, partially offset by the 1Q97 gain of approximately $100 million or about $0.04 per share after tax on the sale of AT&T Skynet. The 1Q98 gains totaled $667 million pre-tax, or approximately $0.26 per share after tax.

EBIT and EBITDA increased 15.7% and 13.3%, respectively from 1Q97. The impact of the sales of ASCC and LIN-TV was largely offset by the write-down of assets associated with the resale of local services. Excluding the write-down of local assets, a non-cash item, EBITDA increased 35%.

Interest expense was $48 million in the first quarter, down 6.4% from the year-ago quarter.

Provision for income taxes was up 8.9% from 1Q97, with an effective tax rate of 35.6%. The effective tax rate decreased 240 basis points from 1Q97, primarily as a result of foreign legal entity restructurings.

Income from discontinued operations was $10 million net of taxes, down from $38 million in 1Q97. This quarter, discontinued operations included the results of AT&T Universal Card; in the year-ago quarter the results of AT&T Submarine Systems were also included in discontinued operations.

Net income increased 17.8% from 1Q97. The impact of the local write-down largely offset the gains from the sales of LIN-TV and ASCC.

Earnings per share were $0.81 on a consolidated basis, up 17% from $0.69 in the year-ago quarter. AT&T has targeted a range of $3.25 - $3.35 per share for 1998 including TCG.

See Appendix I for the full AT&T income statement, and Appendix II for complete restated income statements.

Balance Sheet and Capital Discussion

Total assets decreased $1,730 million, or 3.0%, primarily due to declines in property, plant, and equipment, other receivables and investments. The decrease in property, plant and equipment is primarily a result of the local asset impairment charge and the sale of AT&T Solutions Customer Care. Other receivables, which represent financing of AT&T Universal Card receivables by AT&T, decreased due to lower cardholder receivables resulting from the paydown of holiday spending balances. The decrease in investments reflects the sale of LIN-TV.

Total liabilities decreased $2,363 million, or 6.6%, primarily due to declines in debt, payroll and benefit-related liabilities, accounts payable and long-term deferred taxes, partially offset by an increase in current liabilities. The decreases in both short-term and long-term debt reflect the paydown of debt with the proceeds from the sales of LIN-TV and AT&T Solutions Customer Care, as well as lower debt requirements at Universal Card resulting from lower cardholder receivables. The decrease in payroll and benefit-related liabilities reflects the annual first quarter payout of employee bonuses. Accounts payable declined primarily due to the paydown of high year-end payables mostly capital related. The decrease in long-term deferred taxes is primarily due to the write-down of local assets as well as benefits related to a foreign legal entity restructuring. The increase in current liabilities was driven by higher current accrued income taxes which include the impact of the ASCC and LIN-TV sales.

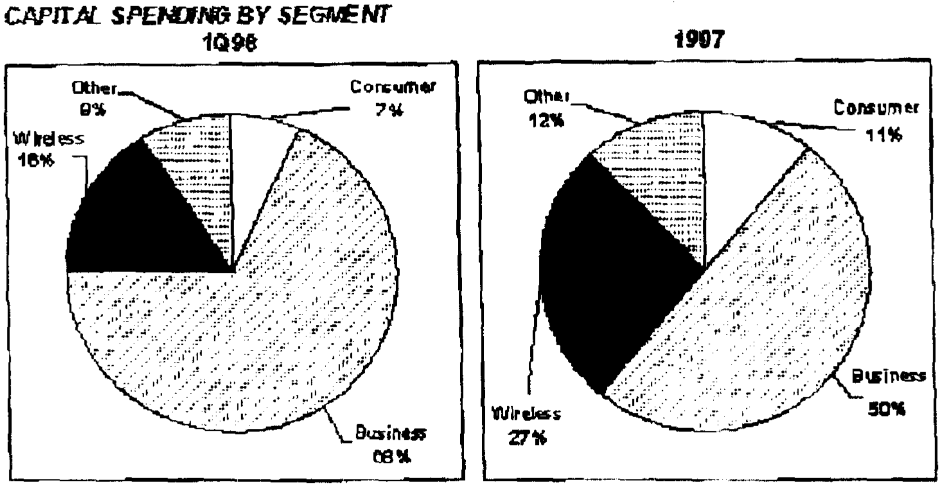
Total shareowner equity increased $633 million, or 2.8%, primarily due to the current quarter's net income partially offset by dividends declared.

AT&T's debt ratio, defined as total debt divided by total capital was 28.2% including debt related to Universal Card. AT&T's debt ratio net of cash was 27.7% as of March 31, and is expected to decline to less than 10% after the AT&T Universal Card sale to Citibank, which closed on April 2, 1998.

Capital additions were $1,046 million in the first quarter, a decrease of 12.6% compared to 1Q97. Capital additions included $992 million of capital expenditures. Capital was directed primarily at investment in AT&T's long-distance network, including the continuing deployment of SONET rings and buildout of the digital wireless network. AT&T expects to complete its SONET deployment in 1998.

AT&T's full consolidated balance sheets appear in Appendix V.

CAPITAL SPENDING BY SEGMENT



Business Segment Discussion

AT&T's results are segmented according to the company's primary lines of business: business services, consumer services, and wireless services. A fourth segment, identified as other/corporate, includes the results of AT&T Solutions, international operations and ventures, on-line services such as AT&T WorldNet Internet access, and various other items. The results of these four segments plus the impact of the elimination of internal business sum to AT&T's total results. The following is a discussion of each of these segments, as well as supplemental information on local service, AT&T Solutions, international operations and ventures, on-line services, and new wireless businesses.

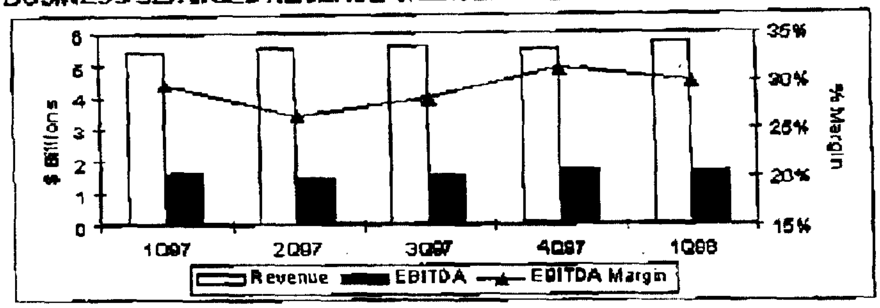
Total assets by segment include all external assets for each segment except for deferred taxes and prepaid pension assets which are held at the corporate level. Network assets are allocated to the segments based on the prior three years' volumes and are reallocated each January.

BUSINESS SERVICES SEGMENT

Business services results reflect sales of long-distance services (domestic and international, inbound and outbound, inter- and intra-LATA toll services, calling card and operator-handled services, data services, messaging and other network enabled services), local services and web hosting and other electronic commerce services.

Total revenue from business services increased 4.5% in the first quarter compared to 1Q97, driven primarily by strong growth in revenue from data services. Data services revenue grew in the low double digits for the quarter, as AT&T again expanded its industry-leading market share position in frame relay service with growth in excess of 100%. Revenue from private line data services continued to grow at a high-single-digit rate. The growth rates of data revenue and overall business segment revenue continue to be impacted by the sales of AT&T Skynet and AT&T Tridom in the first and second quarters of 1997, respectively. Adjusted for those sales, data services revenue grew in the mid teens for the quarter, while total business services revenue grew 5.3%.

BUSINESS SERVICES REVENUE & EBITDA TREND



Business long-distance services revenue, which includes data revenue, grew 4.4% in the quarter, or 5.2% adjusted for the impacts of AT&T Skynet and Tridom. Data revenue was approximately 25% of business long-distance services revenue this quarter, up from a year ago. Revenue from voice services continued to be pressured by price competition, particularly on inbound services, and by substitution of alternate services such as wireless for higher-priced services such as calling cards. Price reductions made in anticipation of access rate reductions also impacted revenue growth, though they were partially offset by the flow-through of USF/PICC charges to customers. Long-distance calling volume grew in the low double digits for the quarter, driven by double-digit growth in inbound services. Volume grew at a slower rate than in recent quarters, primarily as a result of very strong growth a year ago resulting from stimulation due to contract renegotiations as well as additional volume of government traffic under the FTS 2000 contract.

EBITDA for business services increased $90 million, or 5.6% over the year-ago quarter. However, 1Q97 included a gain of approximately $100 million on the sale of AT&T Skynet. Absent that effect, EBITDA increased 12.4% driven by revenue growth and helped by improvements in cost structure related to customer care and sales support. EBIT increased $13 million, or 1.1%, and was up 10.0% when adjusted for the sale of Skynet. Higher levels of depreciation due to AT&T's investment in data networks and SONET deployment accounted for the slower rate of EBIT growth as compared to EBITDA.

Business Services Summary					
	1Q98	1Q97	Yr/Yr %	4Q97	Seq %
Revenue	$5,673	$5,428	4.5%	$5,485	3.4%
EBITDA	1,694	1,604	5.6%	1,713	(1.1)%
EBITDA Excluding Gain on Skynet	*1,694*	*1,507*	*12.4%*	*1,713*	*(1.1)%*
EBITDA Margin (adjusted)	*29.9%*	*27.8%*	*210 b.p.*	*31.2%*	*(130) b.p.*

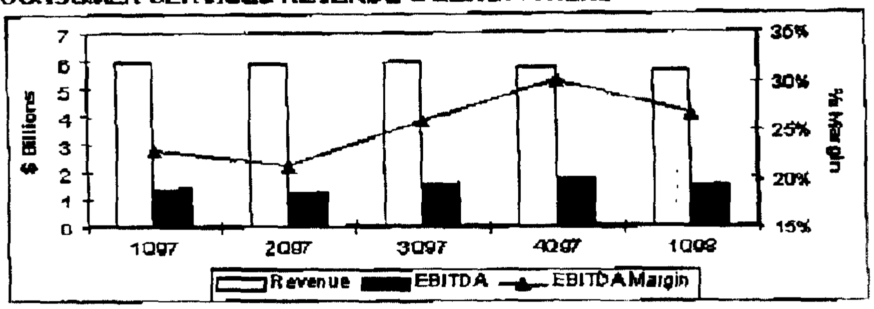
EBIT	1,206	1,193	1.1%	1,238	(2.6)%
EBIT Excluding Gain on Skynet	*1,206*	*1,096*	*10.0%*	*1,238*	*(2.6)%*
EBIT Margin (adjusted)	*21.3%*	*20.2%*	*110 b.p.*	*22.6%*	*(130) b.p.*

Capital additions for business services totaled $711 million in the quarter, primarily reflecting investment in data networks, AT&T's SONET program and the AT&T Digital Link product for local service. *Total assets* for business services were $15.4 billion as of March 31.

CONSUMER SERVICES SEGMENT

AT&T's consumer services segment includes the results of providing long-distance services (including domestic and international, inter- and intra-LATA toll services, calling card and operator handled calling, and prepaid calling cards) and local services to residential customers.

CONSUMER SERVICES REVENUE & EBITDA TREND



Revenue from consumer services decreased 5.1% in the first quarter, as *consumer long-distance services revenue* declined 5.5% on a slight decline in calling volume. The decline in revenue resulted in part from access cost reductions implemented in July 1997, which enabled AT&T to lower basic rates and move many customers to more favorable optional calling plans. The controlled migration of customers to more favorable calling plans is a key part of AT&T's strategy to retain profitable customers. In addition, the reduction in revenue reflects the continuation of AT&T's high-value targeting strategy, implemented in the second half of 1997, under which AT&T stopped targeting non-profitable customers for acquisition. These changes continue to have an impact on revenue and volume growth, but contribute to improved profitability and customer retention. Competition in the residential long-distance market, as well as substitution away from higher-priced services such as calling cards toward wireless services, also contributed to the lower revenue and volume growth rates. Higher intra-LATA revenue and volume, which has resulted from AT&T's aggressive localized marketing efforts in areas where pre-subscription is available, partially offset these revenue and volume effects.

EBITDA and EBIT for consumer services increased 10.3% and 11.8% respectively, over the year-ago quarter, driven primarily by reduced SG&A expenses. These reductions are a reflection of AT&T's plan to target and retain the most profitable residential customers. SG&A reductions included significantly lower marketing and sales expenses as a result of better targeting and efficiency gains in customer acquisition efforts. AT&T has also increased its use of alternate distribution channels, including the launch of One Rate On-line, and honed its customer retention techniques through database mining and consolidation of marketing messages. As a result, spending on telemarketing and direct mail declined compared to the year-ago quarter. Sequentially, EBIT declined 13.0% due primarily to the traditionally higher marketing activity of the first quarter compared to the fourth and to the normal post-holiday decline in long-distance revenue.

Consumer Services Summary					
	1Q98	1Q97	Yr/Yr %	4Q97	Seq %
Revenue	$5,628	$5,928	(5.1)%	$5,749	(2.1)%
EBITDA	1,498	1,358	10.3%	1,725	(13.2)%
EBITDA Margin	26.6%	22.9%	370 b.p.	30.0%	(340) b.p.
EBIT	1,324	1,184	11.8%	1,522	(13.0)%
EBIT Margin	23.5%	20.0%	350 b.p.	26.5%	(300) b.p.

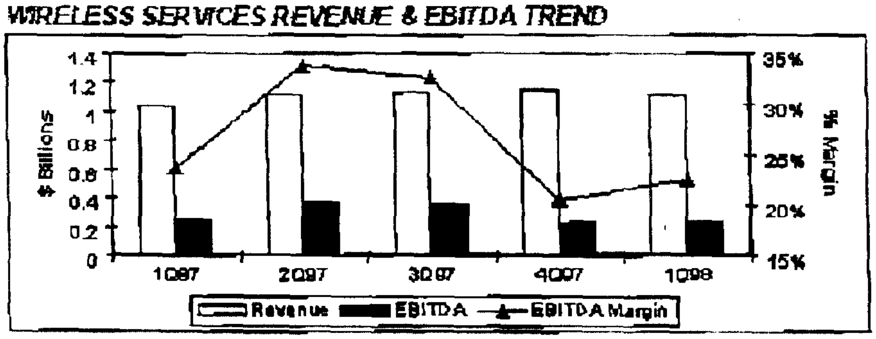
Capital additions for consumer services were $76 million in the quarter. *Total assets* for consumer services were $7.0 billion at March 31.

WIRELESS SERVICES SEGMENT

The results of this segment are comprised primarily of sales of wireless services and products to customers in 850 MHz cellular markets and newer 1.9 GHz wireless markets. Also included are the results of the messaging, aviation communications, and wireless data divisions, as well as the costs associated with the development of fixed wireless technology. Charges related to AT&T's decision to exit the two-way messaging business are included in the results for 1Q97. These charges totaled $160 million, including $80 million of depreciation and amortization expense and $80 million of network and other communications services expense.

The impact of the new 1.9 GHz markets, wireless data, two-way messaging and fixed wireless development are reflected here as "new wireless businesses"; all other wireless results are reflected as "core" businesses.

WIRELESS SERVICES REVENUE & EBITDA TREND



Total revenue from wireless services increased 7.0% compared to 1Q97. The increase was driven by growth in revenue from both core and new wireless businesses, with revenue growth trending upward throughout the first quarter. Core revenue increased 4.3% to $1,083 million, while revenue from new businesses was $30 million for the quarter compared to $2 million in the year-ago quarter. Consolidated subscribers—those in markets in which AT&T owns a controlling interest—totaled 6.159 million at March 31. This represents an increase of 16.9% over March 31, 1997, on net adds of approximately 195,000. Consolidated subscribers include well over 100,000 users in AT&T's ten emerging 1.9 GHz markets. The tenth market—Boston/Providence—was launched during the first quarter. These markets represent approximately 70% of the total POPs covered by AT&T's 1.9 GHz licenses. Also during the quarter, AT&T announced joint ventures with Cincinnati Bell and Telecorp to further increase its digital coverage.

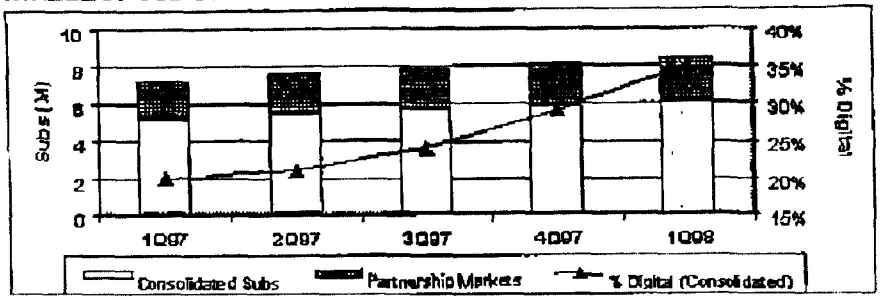
Wireless Services—Total Summary					
	1Q98	**1Q97**	**Yr/Yr %**	**4Q97**	**Seq %**
Revenue	$1,113	$1,040	7.0%	$1,155	(3.7)%
EBITDA	251	246	2.2%	238	5.8%
EBITDA Excluding Charge	*251*	*326*	*(22.9)%*	*238*	*5.8%*
EBITDA Margin (Adjusted)	*22.6%*	*31.4%*	*(880) b.p.*	*20.6%*	*200 b.p.*
EBIT	(2)	(31)	94.0%	(5)	57.1%
EBIT Excluding Charge	*(2)*	*129*	*(101.4)%*	*(5)*	*57.1%*
EBIT Margin (Adjusted)	*(0.2)%*	*12.4%*	*(1,260) b.p.*	*(0.4)%*	*20 b.p.*

In response to the competitive environment of the wireless industry, AT&T has adjusted prices on many of its high-end rate plans in an effort to retain customers. This pricing activity has put downward pressure on AT&T's revenue per user. However, the company has also made a strategic decision not to pursue acquisitions of low-value customers. Partly as a result of this strategy, average revenue per user in core markets declined at a slower rate in the first quarter than in recent quarters—10% year-over-year to $50. This selective acquisition strategy is being applied in new markets as well, with over 70% of customer acquisitions in the quarter purchasing rate plans priced at $50 per month or higher.

At the same time, AT&T has acted aggressively to convert the wireless subscriber base from analog to digital service. This effort increases costs in the near-term; however, digital service is provided at a lower operating cost and is expected to contribute to lower customer churn. As of March 31, 1998, about 35% of AT&T's consolidated subscribers were on digital plans, compared to 29% at the end of 1997 and 20% a year ago.

Wireless services EBITDA was $251 million for the quarter, up 2.2% from the year-ago quarter. EBITDA from new businesses was negative $112 million this quarter, compared to negative $114 million in 1Q97 (including charges of $80 million related to the two-way messaging business). Core wireless EBITDA was up slightly from the year-ago quarter in spite of the costs of migrating customers to digital service. Total wireless EBIT was negative $2 million for the quarter, including negative $156 million from new businesses. In the year-ago quarter, EBIT of negative $31 million included losses of $205 million from new businesses.

WIRELESS SUBSCRIBERS & PERCENT DIGITAL



Wireless Services *New Businesses*	1Q98	1Q97	Yr/Yr %	4Q97	Seq %
Revenue	$ 30	$ 2	N/A	$ 15	94.5%
EBITDA	(112)	(114)	1.7%	(183)	38.8%
EBITDA Excluding Charge	*(112)*	*(34)*	*(228.6)%*	*(183)*	*38.8%*
EBIT	(156)	(205)	23.7%	(203)	23.0%
EBIT Excluding Charge	*(156)*	*(45)*	*(248.2)%*	*(203)*	*23.0%*

Wireless Services *Subscribers* (thousands)	1Q98	1Q97	Yr/Yr %	4Q97	Seq %
Consolidated Markets	6,159	5,270	16.9%	5,964	3.3%
Net Additions	195	251	(22.6)%	234	(16.8)%
Partnership Markets	2,212	1,991	11.1%	2,169	2.0%
Total Subs	8,371	7,261	15.3%	8,133	2.9%
Messaging Subscribers	1,329	1,185	12.2%	1,300	2.2%

Capital additions for wireless services totaled $168 million in the quarter. Capital was directed primarily at expanding coverage in new and traditional markets. Total assets for wireless services were $18.3 billion at March 31.

OTHER/CORPORATE

This segment includes the results of AT&T Solutions, international operations and ventures, on-line services such as AT&T WorldNet, and other corporate operations. Results for this segment are discussed briefly here; a more detailed discussion of certain components of the segment appears in the supplemental disclosure section below.

Other/corporate revenue increased 21.1% over 1Q97, driven by increased revenue from AT&T Solutions and AT&T WorldNet. EBITDA and EBIT increased 29.7% and 19.3%, respectively as a result of the gains on the sales of AT&T Solutions Customer Care and LIN TV, partially offset by the charge for the local asset impairment. Adjusting for the effects of these items, EBITDA for the segment was negative $385 million, an improvement of 15.4% over negative $454 million in 1Q97. EBIT was negative $501 million, an improvement of 7% over negative $538 million in 1Q97. Lower dilution from international operations and ventures, AT&T WorldNet Services and AT&T Solutions were the primary drivers of the improvement.

Other/Corporate Summary					
	1Q98	1Q97	Yr/Yr %	4Q97	Seq %
Revenue	$557	$460	21.1%	$665	(15.9)%
EBITDA	(319)	(454)	29.7%	(540)	40.9%
EBITDA Excluding Gains & Charges	*(385)*	*(554)*	*30.5%*	*(540)*	*28.6%*
EBIT	(435)	(538)	19.3%	(643)	32.4%
EBIT Excluding Gains & Charges	*(501)*	*(638)*	*21.5%*	*(643)*	*22.1%*

ELIMINATIONS

This "segment" reflects the elimination revenue and profit generated by the sale of services between business segments, such as the sale of long-distance transport services from business services to AT&T Solutions.

1Q98 Segment Recap						
	Business	Consumer	Wireless	Other	Elims	Total
Revenue	$5,673	$5,628	$1,113	$557	($340)	$12,631
EBITDA	1,694	1,498	251	(319)	(3)	3,121
EBIT	1,206	1,324	(2)	(435)	(3)	2,090
Capital Additions	711	76	168	91	-	1,046
Total Assets-Cont. Ops	15,391	7,031	18,277	15,187	-	55,886

SUPPLEMENTAL DISCLOSURE—AT&T Solutions, Worldnet and Other On-line Services, International Operations and Ventures, Local Services

AT&T Solutions, the company's outsourcing, network integration, and multi-media call center business, grew revenue 39.3% in the first quarter to $218 million. The unit currently has more than $3 billion under contract with such clients as United Healthcare, Textron, J.P. Morgan, Merrill Lynch, and MasterCard International. In the first quarter of 1998 AT&T Solutions signed contracts worth about $1 billion for major global data networking services with Citicorp and McGraw-Hill. These contracts did not impact 1Q98 revenue. Although not included in the unit's revenue, AT&T Solutions manages AT&T's internal network infrastructure, an operation that provides information technology services which generated $386 million in internal billings for the quarter.

EBIT for AT&T Solutions was negative $12 million for the quarter, an improvement from negative $53 million in 1Q97. Included in the $12 million was the impact of the realignment of certain start-up network management contracts into the outsourcing practice of AT&T Solutions. AT&T Solutions achieved a significant year-over-year improvement in EBIT as a result of revenue growth and lower

SG&A expense, and remains on target to turn profitable by the end of 1998.

AT&T Solutions Summary					
	1Q98	1Q97	Yr/Yr %	4Q97	Seq %
Revenue	$218	$156	39.3%	$239	(9.1)%
Internal Billings to AT&T*	386	463	(16.7)%	423	(8.7)%
EBITDA	21	(16)	229.2%	22	(1.3)%
EBIT	(12)	(53)	77.6%	(14)	18.4%

*Cost recovery

WorldNet and other on-line services include AT&T WorldNet Internet access service for residential and business customers (included in the corporate/other segment) and web hosting and other electronic commerce services (included in the business services segment). Revenue from on-line services increased 97.4% compared to 1Q97 to $79 million. The increase was due primarily to continued growth in AT&T WorldNet's residential subscriber base, which now totals about 1.1 million. Average revenue per customer continues to increase due to the expiration of AT&T WorldNet's initial promotional price programs in favor of regular monthly rates of $9.95 and $19.95.

EBIT and EBITDA from on-line service both improved as a result of the revenue improvement and network and customer care cost efficiencies for AT&T WorldNet.

WorldNet & Other On-line Services Summary					
	1Q98	1Q97	Yr/Yr %	4Q97	Seq %
WorldNet Subs (k)	1,085	884	22.7%	1,020	6.4%
Hosted Websites (k)	8.1	3.1	163.8%	6.9	16.4%
Revenue	79	40	97.4%	67	15.8%
EBITDA	(95)	(152)	37.7%	(109)	12.9%
EBIT	(109)	(159)	31.7%	(118)	8.1%

International operations and ventures include AT&T's consolidated foreign operations such as AT&T Communications Services UK, the company's transit and reorigination businesses, and its online services in the Asia/Pacific region. This area does not include bilateral international long-distance traffic. The equity earnings or losses of AT&T's non-consolidated international joint ventures and alliances, such as Alestra in Mexico, AT&T Canada Long Distance Services, AT&T – Unisource and World Partners Company are also included in this section.

Revenue from consolidated international businesses increased 20.7% from 1Q97 to $179 million, driven by growth in reorigination and Comms UK. This growth includes the impact of revenue declines in businesses which were non-strategic to AT&T, some of which were exited since 1Q97. Revenue from continuing strategic international operations grew 53.4% compared to 1Q97.

EBIT from international operations and ventures was negative $63 million for the quarter, an improvement of over 50% from 1Q97. The improvement was driven primarily by increased revenue and operational improvements in consolidated international operations and by reductions of costs required to support both consolidated and non-consolidated international operations. Revenue generated by non-consolidated ventures and alliances was $785 million for the quarter, up 27% from a year ago as a result of volume growth across all of the major businesses.

International Operations & Ventures Summary					
	1Q98	1Q97	Yr/Yr %	4Q97	Seq %
Revenue	$179	$148	20.7%	$218	(18.2)%
EBITDA	(46)	(114)	60.2%	(39)	(16.9)%
EBIT	(63)	(128)	50.8%	(56)	(12.2)%

*Local services*for business and residential customers are included as part of AT&T's business services and consumer services segments, discussed above. The table below includes the results of business and consumer local services as well as the costs associated with corporate staff dedicated to AT&T's local services effort. (These costs are reported as part of the Other/Corporate business segment.)

Revenue from local services, primarily comprised of AT&T Digital Link (ADL) service for business customers and services sold to residential customers on a total service resale (TSR) basis was $37 million, up from $4 million in 1Q97. AT&T currently offers ADL as an outbound local calling service in 49 states, and as an outbound and inbound service in New York, Connecticut, New Jersey, and California. Local number portability, key to the provisioning of competitive local exchange services, remains an obstacle to AT&T's progress in offering fully functional business local services. AT&T's pending merger with TCG is designed to accelerate the company's penetration of the business local exchange market.

AT&T continues to provide local service on a TSR basis to about 400,000 residential customers in six states. However, the company has ceased marketing TSR services due to the unfavorable wholesale pricing structure currently in place. AT&T continues to seek alternative methods of providing local service to residential customers.

EBITDA and EBIT for local services include the $601 million asset impairment charge. Adjusting for this charge, EBITDA decreased by $52 million and EBIT by $66 million reflecting costs associated with growth in ADL and TSR. Losses related to residential local services are expected to decline as the company further limits its TSR activities.

Total assets and capital spending for local service are primarily related to AT&T Digital Link and other facilities-based local service options.

Local Services Summary					
	1Q98	1Q97	Yr/Yr %	4Q97	Seq %
Revenue	$ 37	$ 4	779.3%	$ 39	(5.4)%
EBITDA	(781)	(128)	(512.9)%	(267)	(192.1)%
EBITDA Excluding Charge	*(180)*	*(128)*	*(41.4)%*	*(267)*	*32.6%*
EBIT	(805)	(138)	(483.9)%	(293)	(174.4)%
EBIT Excluding Charge	*(204)*	*(138)*	*(48.1)%*	*(293)*	*30.4%*

New wireless businesses

Information related to AT&T's new wireless businesses is included in the wireless services segment discussion.

Appendices

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Merrill Lynch

In-depth Report

United States
Telecommunications/Services

4 March 1998

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Long Distance

Surging Demand for Data Partially Offset Long Distance Pricing Pressure and Share Loss

Reason for Report: Fourth Quarter Review

Industry

Investment Highlights:

- **Fourth quarter results were mixed for the long distance companies. Despite a slight improvement in core results, the Big 3's consolidated EPS continued to suffer as a result of dilutive new initiatives (i.e., local, PCS, data, global alliances).**
- **Despite numerous price increases and huge growth in data/Internet transmissions, long distance price pressures more than doubled in '97 – the average rate per minute (or "Gap") fell 6.5% versus 2.2% in 1996. The Gap in 4Q97 was -8.0%, down from -7.8% in 3Q and 4Q96's -2.8%.**
- **The long distance market share shift continued through 4Q – as evidenced by the disparity of the revenue growth statistics between the Big 3 and second tier players. The average revenue growth rate for the Big 3 dropped from 7.2% in 1996 to 2.6% in 4Q97 – compared with average second tier company growth rates of over 20% in 1996 and 31% in 4Q.**
- **We have seen a number of new, low rate long distance products offered by various providers which should put further pressure on pricing. Despite distribution efficiencies, these products could generate lower profit per minute even while they enhance margin on a percentage basis.**
- **The acquisition of Teleport finally launched AT&T into the local market, although even with the CLEC's $1.8 billion of local assets, AT&T's national local exposure is still limited. AT&T says Teleport's assets will address only 28% (or $21 billion) of the $75 billion local market (excluding approx. $25 billion of access revenues), thus leaving the remaining $54 billion to be addressed by resale and unbundling strategies, which thus far have proved to be uneconomic and/or extremely difficult to implement.**
- **Our investment choices are limited to special situations (WorldCom and Frontier) and selected start-ups (Qwest and RSL Communications).**

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